
2003

Nebraska S Corporation Income Tax Booklet



Questions?

Call Taxpayer
Assistance

1-800-742-7474

(toll free in NE or IA)
or **1-402-471-5729**.

Included in this Booklet:

Form 1120-SN, Schedules
I, II, and III, and Business
Classification Codes.

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2003 Nebraska S Corporation Income Tax

INSTRUCTIONS

An S corporation whose shareholders are all Nebraska residents and which derives all of its income from Nebraska is **not** required to file a Nebraska S Corporation Income Tax Return, Form 1120-SN. Its shareholders report their share of the S corporation income and any bonus depreciation add-back on their Nebraska income tax returns.

BONUS DEPRECIATION AND ENHANCED SECTION 179 EXPENSE DEDUCTION. Due to passage of LB 596 by the 2003 Nebraska Legislature, S corporations must report any federal bonus depreciation and enhanced Section 179 expense deduction to their shareholders. The shareholders will have to add back 85 percent of their share of the bonus depreciation and 100 percent of their share of the enhanced Section 179 expense deduction on their individual income tax returns. Any amount added back may be reclaimed in a later year. Twenty percent of the 2003 add-back may be subtracted in the first taxable year beginning on or after January 1, 2006, and 20 percent in each of the next four taxable years.

Reminder: For tax years 2001 and 2002 partners must add back 85 percent of their share of the S corporation's bonus depreciation claimed in those years. Twenty percent of the tax year 2001 and 2002 bonus depreciation added back may be subtracted in the first taxable year beginning on or after January 1, 2005, and 20 percent in each of the next four taxable years.

The passage of LB 608 changed several provisions of the Employment Expansion and Investment Incentive Act (LB 270). Beginning January 1, 2004, entities wishing to receive benefits under this Act must submit an application and a \$500 fee to this department. Applications will be reviewed in the order they are received. Qualifying projects will be approved provided the total expected credits for all approved projects under this Act are less than \$2,500,000. For additional information visit our Web site at www.revenue.state.ne.us and click on Tax Incentives.

NOTE: The department has changed its method of distributing S Corporation Income Tax booklets. **If you wish to receive a printed booklet from the department next year, you must check the box at the top of Form 1120-SN.** Otherwise, you may obtain a copy from your accountant, at any of our offices throughout Nebraska, or you may download the forms and instructions from our Web site: www.revenue.state.ne.us.

WHO MUST FILE. Every S corporation as defined by Section 1361 of the Internal Revenue Code must file a Nebraska S Corporation Income Tax Return, Form 1120-SN, unless all shareholders are residents of Nebraska, and all income is derived from Nebraska sources.

Financial institutions which maintain a permanent place of business in this state and actively solicit deposits from residents of this state must file a Nebraska Financial Institution Tax Return, Form 1120NF. Financial institutions organized as S corporations, must also file a Nebraska S Corporation Income Tax Return, Form 1120-SN.

WHEN AND WHERE TO FILE. This return must be filed on or before the 15th day of the third month following the close of the taxable year. The return must be filed with the Nebraska Department of Revenue, P.O. Box 94818, Lincoln, Nebraska 68509-4818.

PERIOD TO BE COVERED BY THE RETURN. This return must be filed for the calendar year 2003 or fiscal year beginning in 2003. An S corporation reporting for a fiscal year or filing a short-period return must enter the beginning and ending dates of the taxable year in the space provided at the top of the return. The taxable year for Nebraska must be the same as the year used for federal income tax purposes. If an S corporation changes its federal taxable year, it must change the Nebraska taxable year accordingly. A copy of the approval from the Internal Revenue Service to change accounting periods must accompany the first return which reflects the change. Write "Final Return" at the top of the return if the corporation ceased to exist during the 2003 tax year.

EXTENSION OF TIME. It is not necessary to request a Nebraska extension of time when the S corporation has been

granted an extension to file its federal return. The Nebraska Department of Revenue will accept an approved federal extension of time, provided a copy of the approval is attached to the Nebraska return when filed. By requesting an extension of time to file your federal return using the Application for Automatic Extension of Time to File Corporation Income Tax Return, Form 7004, you are granted a 6-month extension. When a federal extension of time has been granted and additional time is necessary to file the Nebraska return, the Nebraska Form 7004N needs to be filed on or before the date the federal extension expires.

An extension of time to file may be obtained from the Nebraska Department of Revenue even if the S corporation does not request a federal extension of time. The extension must be requested on Application for Automatic Extension of Time to File Nebraska Corporation Income Tax Return, Form 7004N, on or before the due date of the return. If granted, the extension will be for a seven-month period. No further extension can be granted.

NONRESIDENT SHAREHOLDER WITHHOLDING. A nonresident individual shareholder should forward a completed Nebraska Nonresident Income Tax Agreement, Form 12N, to the S corporation before the filing of the Nebraska S Corporation Income Tax Return, Form 1120-SN. The S corporation must attach the completed Form 12N to its return. The Form 12N is an agreement by a nonresident of Nebraska to file a Nebraska Individual Income Tax Return, Form 1040N, and to report and pay Nebraska income tax on Nebraska source income attributable to the taxpayer's interest in an S corporation.

The S corporation is required to withhold Nebraska income tax from each nonresident shareholder for whom a

completed Form 12N is not attached. The amount to be withheld is 6.84 percent of the nonresident shareholder's share of bonus depreciation and enhanced section 179 expense deduction add-back and any taxable income which was derived from or attributable to sources within Nebraska. The S corporation must report the amount withheld from each nonresident shareholder on the Statement of Nebraska Income Tax Withheld for Nonresident Individual, Form 14N. Attach the white copy of each Form 14N to the S corporation return.

The nonresident individual shareholder may claim the amount withheld as a credit against his or her Nebraska income tax liability by attaching a copy of the Form 14N to the Nebraska Individual Income Tax Return, Form 1040N.

The Form 12N and Form 14N requirements apply only to nonresident **individual** shareholders. Shareholders other than individuals are not subject to the nonresident shareholder withholding requirements.

If a nonresident shareholder's only connection with Nebraska is conduct of the business activities of the S corporation and the corporation has withheld tax from any bonus depreciation and enhanced Section 179 expense deduction add-back and all the Nebraska income attributable to the nonresident's share of the organization's income, the nonresident shareholder does not have to file a return. The full amount of the withholding is, at the taxpayer's option, retained in lieu of the filing of an individual income tax return. Any nonresident who so desires can still file a return and claim a refund if there is one due. Any nonresident who filed Form 12N to avoid withholding must file Form 1040N.

PAYMENT OF TAX WITHHELD. The entire tax withheld from the nonresident shareholders is required to be paid on or before the original due date of the return. Make check or money order payable to the Nebraska Department of Revenue. Write the Nebraska identification number on the face of the remittance. Payment can also be made by electronic funds transfer (EFT), or by credit card. Details for these payment options can be found on the department's Web site at www.revenue.state.ne.us. An extension of time to file Form 1120-SN does not extend the date for payment of tax. Checks written to the Department of Revenue may be presented for payment electronically.

PENALTIES AND INTEREST. Penalties may be imposed for failure to file a complete return, failure to file a timely return, or failure to file an amended return when required. Any unpaid tax is subject to interest at the statutory rate from the original due date to the date the tax is paid.

QUALIFIED SUBCHAPTER S SUBSIDIARIES. Any subsidiary of an S corporation which is treated as a Qualified Subchapter S Subsidiary (QSSS) for federal income tax purposes will be treated in the same manner for Nebraska income tax purposes. All of the assets, liabilities, and items of income, deduction, and credit of the QSSS will be considered to be those of its parent.

AMOUNTS INCLUDED IN THE RETURN OF THE SHAREHOLDER. Both resident and nonresident

shareholders are subject to the Nebraska income tax on their share of the S corporation's bonus depreciation, enhanced Section 179 expense deduction, and income derived from or attributable to sources within Nebraska.

REPORT OF NEBRASKA SOURCE INCOME TO SHAREHOLDERS. An S corporation must provide all shareholders with a schedule listing the amount and type of income, deductions, bonus depreciation, and enhanced Section 179 expense deduction, that are to be included in the shareholder's Nebraska tax return.

A Federal Schedule K-1 may be used for each shareholder, provided it is modified to include the shareholder's share of U.S. government interest, state and local obligations, bonus depreciation, and enhanced Section 179 expense deduction. The amounts reported on the K-1 must be calculated in the same manner as income is distributed.

For S corporations apportioning income, the amount of **Nebraska** income, bonus depreciation, and enhanced Section 179 expense deduction must also be provided to each shareholder together with a copy of the Nebraska Schedule I, Form 1120-SN.

If the S corporation is a member of a unitary group, the S corporation is deemed to be doing business within this state if any part of its income is derived from transactions with other members of the unitary group doing business within this state. Such corporation shall apportion its income, bonus depreciation, and enhanced Section 179 expense deduction by using the apportionment factor determined for the entire unitary group, including the S corporation.

For S corporations using an alternative method to determine income attributable to Nebraska, the amount reportable to the shareholder will be determined in accordance with the method previously approved by the State Tax Commissioner.

ACCOUNTING METHODS. The method of accounting used for federal income tax purposes must be used for Nebraska income tax purposes. The taxpayer may not change the method of accounting used in reporting income in prior years unless the change is approved by the Internal Revenue Service. A copy of this approval must accompany the first return which reflects the change in the method of accounting.

ROUND TO WHOLE DOLLARS. Round any amount from 50 cents through 99 cents to the next higher dollar. Round any amount less than 50 cents to the next lower dollar. The amounts on the return and schedules are to be shown in whole dollars.

FEDERAL RETURN. A copy of the actual federal return and supporting schedules as filed with the Internal Revenue Service must be attached to this return.

CHANGES OR CORRECTIONS ON FEDERAL RETURN OR ANOTHER STATE'S RETURN. Any corporation whose reported income or deductions are changed or corrected by the Internal Revenue Service or through a renegotiation of a contract with the United States is required to report the change or correction to the Nebraska

Department of Revenue within 90 days of the determination by filing a Nebraska S Corporation Income Tax Return, Form 1120-SN, clearly marked "Amended" at the top of the return. In addition, any corporation whose reported income or allowable tax credit in another state is changed or corrected by that state or any other competent authority in a way material to the tax liability owed to Nebraska is required to report the change or correction within 90 days after it becomes final by filing Form 1120-SN, clearly marked "Amended" at the top of the return.

Any corporation which filed an amended return with the Internal Revenue Service or which filed an amended return with another state involving a change or correction material to its Nebraska tax liability must file an amended return with the Nebraska Department of Revenue within 90 days of the filing of the amended federal or state return.

Any change or correction reported must be mailed separately from the annual return of the corporation.

NONHIGHWAY USE MOTOR VEHICLE FUELS. An S corporation which purchases nonhighway use motor vehicle fuels will distribute its qualified gallons to its shareholders. Computation of qualified gallons and the distribution to the shareholders is done on the Nebraska Nonhighway Use Motor Vehicle Fuels Credit Computation, Form 4136N, which is available from the Department of Revenue and most banks. The Form 4136N must be attached to Form 1120-SN and a copy provided to each shareholder.

A Nebraska S Corporation Income Tax Return, Form 1120-SN, is **not** required when all the shareholders are Nebraska individual residents **and** all the S corporation income is from Nebraska even though the S corporation has a Nonhighway Use Motor Vehicle Fuels Credit to distribute to its shareholders. The shareholders will report their share of the S corporation income or nonhighway motor fuel credit by filing their own Nebraska income tax return and attaching a copy of the S corporation's Form 4136N.

For more information, contact Taxpayer's Assistance toll free at 1-800-742-7474 in Nebraska and Iowa, or 1-402-471-5729.

NEBRASKA COMMUNITY DEVELOPMENT ASSISTANCE ACT CREDIT. This credit is allowable for contributions to approved projects of community betterment organizations recognized by the Nebraska Department of Economic Development. See the instructions on the 2003 Nebraska Community Development Assistance Act Credit Computation, Form CDN, for more information on this credit. Form CDN and a copy of Form 1099NTC must be attached to the Form 1120-SN and a copy provided to each shareholder.

Each shareholder of an electing S corporation shall report his or her share of the credit in the same manner and proportion as he or she reports the S corporation income. More detailed information on this credit can be obtained by writing to the Nebraska Department of Economic Development, Community and Rural Development Division, P.O.

Box 94666, Lincoln, Nebraska 68509-4666; or by calling 1-402-471-4169 or 1-800-426-6505, extension 4169.

BEGINNING FARMER CREDIT, is the credit available to owners of agricultural assets which are rented to qualifying beginning farmers or livestock producers. Each shareholder eligible for the credit will receive a copy of the Certificate of Nebraska Tax Credit, Form 1099 BFC, from the Nebraska Department of Agriculture. To claim their share of the credit, eligible shareholders must file Form 1099 BFC with their income tax return. **Form 1099 BFC is not filed with Form 1120-SN.** For detailed information on this credit, contact the Nebraska Department of Agriculture, P.O. Box 94947, Lincoln, NE 68509-4947, or call 1-402-471-6890 or 1-800-446-4071.

EMPLOYMENT AND INVESTMENT GROWTH CREDIT. This credit is allowable for additional investment and employment in Nebraska. For more information, see the instructions on the Nebraska Employment and Investment Credit Computation, Form 3800N. Form 3800N must be attached to the Form 1120-SN, and a copy provided to each shareholder if this credit is allowed to the shareholders.

More detailed information on these credits can be obtained on our Web site at www.revenue.state.ne.us or by contacting the Nebraska Department of Revenue, P.O. Box 94818, Lincoln, Nebraska 68509-4818, or by calling the Lincoln regional office at 1-402-471-5729, or dial 1-800-742-7474 in Nebraska and Iowa.

SIGNATURES. This return must be signed by a corporate officer. If the S corporation authorizes another person to sign the return, there must be a power of attorney on file with the Nebraska Department of Revenue.

Any person who is paid for preparing a taxpayer's return must also sign the return as preparer.

DEFINITIONS.

1. **Apportionment** means the process of determining the portion of income derived from sources within a state. The entire federal taxable income of a unitary business operating within and without Nebraska is presumed subject to apportionment.
2. **Bonus depreciation** means the special depreciation allowance for certain property pursuant to provisions of the Internal Revenue Code.
3. **Enhanced Section 179 expense deduction** means the expense in excess of \$25,000 allowed pursuant to provisions of the Internal Revenue Code.
4. **Sales** means all gross receipts of the taxpayer.
5. **Single economic unit** means a business where there is a sharing or exchange of value between the parts of the unit. A sharing or exchange of value occurs when the parts of the business are linked by a) common management or b) common operational resources that provide material economies of scale

or transfers of value or flow of goods, capital, or services between the parts of the unit.

6. **State** means any state of the United States, the District of Columbia, the Commonwealth of Puerto Rico, any territory or possession of the United States, and any foreign country or political subdivision thereof.

SPECIFIC INSTRUCTIONS

BUSINESS CLASSIFICATION CODE. Enter the number from the Business Classification Code list in this booklet that best describes your principal business activity. **Please review your code carefully.**

ALL S CORPORATIONS which are required to file a Form 1120-SN must complete lines 1 through 6. Lines 7 through 18 are completed only if the S corporation has nonresident individual shareholders and its line 6 entry is not a loss.

LINE 4. Enter line 20 of Nebraska Schedule II. Federal income taxes paid cannot be deducted as an adjustment decreasing federal taxable income.

LINE 6. If all income is derived from sources within Nebraska, enter the amount from line 5, Form 1120-SN.

S corporations deriving income from sources within and without Nebraska shall enter the amount from line 3, Nebraska Schedule I.

LINE 12. If there is recapture of Employment Expansion and Investment Incentive Act (LB 270) credits entered on line 36 of Form 3800N, also enter that amount on line 12 of Form 1120-SN.

LINE 14. Enter the amount of taxes deposited with Form 7004N. Also include any amounts that were paid as estimated taxes for 2003 for any S corporation which is included on this return. Please note that there is no requirement that S corporations remit estimated taxes and no penalty for failure to do so. Do not include any Nebraska withholding reported on Form 1099-MISC which was withheld on payments for nonresident personal services performed by shareholders of the S corporation.

INSTRUCTIONS FOR NEBRASKA SCHEDULE I Apportionment of Income

Nebraska Schedule I must be completed by all S corporations which derive income from sources both within and without Nebraska. Income, bonus depreciation, and enhanced Section 179 expense deduction apportioned to Nebraska are determined by multiplying these items by the calculated apportionment factor. The factor on this schedule must be calculated to at least five decimal places and rounded to four.

Nebraska uses a single factor, sales only, formula to apportion income.

An S corporation using an alternative method of apportionment or separate accounting must attach a copy of the prior approval of either method. The separate accounting calculation or the alternative apportionment factor computation

must be included. Enter the factor on line 2, Nebraska Schedule I.

If the S corporation is a partner in a partnership or joint venture, see Corporate Income Tax Regulation 24-056, Corporation as Partner in a Partnership or Joint Venture.

If an S corporation is a member of a unitary group which includes a C corporation, the apportionment factor for the S corporation will be the apportionment factor as determined for the unitary group. This factor will be applied against the income, bonus depreciation, and enhanced Section 179 expense deduction of the S corporation. **Separate returns must be filed for the S corporation and the C corporation.**

SALES FACTOR. The sales factor is a fraction, the numerator of which is the total sales of the taxpayer in Nebraska during the taxable year, and the denominator of which is the total sales of the taxpayer everywhere during the taxable year. Total sales include gross sales of real and tangible personal property less returns and allowances and all other items of gross receipts which constitute apportionable income. Intercompany sales between unitary corporations using the combined income approach are excluded from the sales factor. Gross receipts, if substantial in amount, realized from an incidental or occasional sale of a fixed asset used in connection with the taxpayer's regular trade or business are excluded from the sales factor since the inclusion of such receipts would not fairly reflect the extent of the taxpayer's business activity in Nebraska.

The following sales of tangible personal property are included as Nebraska sales in the sales factor:

1. Sales of property which are delivered or shipped to a purchaser, other than the U.S. government, within Nebraska regardless of the f.o.b. point or other conditions of the sale;
2. Sales to the U.S. government of property shipped from an office, store, warehouse, factory, or other place of storage in this state;

Sales other than the sales of tangible personal property are in Nebraska if:

1. The income-producing activity is performed in Nebraska; or
2. The income-producing activity is performed both within and without Nebraska and a greater proportion of the income-producing activity is performed in Nebraska during the taxable year than in any other state, based on cost of performance.

Sales or receipts not specifically assigned by the preceding paragraphs shall be assigned as follows:

1. Gross receipts from the sale, rental, or lease of real property are in Nebraska if the real property is located in Nebraska.
2. Gross receipts from the rental, lease, or licensing of the use of tangible personal property are in Nebraska if the property is in Nebraska. If the property was both within and without Nebraska

during the taxable year, then the gross receipts attributable to the period or the percentage of time the property was used in Nebraska are considered in Nebraska.

3. Gross receipts from the performance of services are in Nebraska if the services are performed in Nebraska. If such services are performed partly within and partly without Nebraska, a portion of gross receipts from performance of the services shall be attributed to Nebraska based upon the ratio which the direct costs incurred in Nebraska bears to the total direct costs of the services.
4. Gross receipts from interest or service charges arising from the sale of tangible personal property are attributable to Nebraska if the sale is attributed to Nebraska.

Sales to the U.S. government. The U.S. government is the purchaser when it makes direct payment to the seller. A sale to the U.S. government of tangible personal property is in Nebraska if it is shipped from an office, store, warehouse, or other place of storage in Nebraska. For other sales made to the U.S. government, use the rules stated above for sales of other than tangible personal property.

LINE 13. NEBRASKA APPORTIONMENT FACTOR. To compute the Nebraska apportionment factor, divide line 12, NEBRASKA column, by line 12, TOTAL column, calculate to at least five decimal places and round to four.

INSTRUCTIONS FOR NEBRASKA SCHEDULE II Adjustments to Ordinary Income

Complete Nebraska Schedule II to compute Nebraska adjustments to ordinary income such as income from U.S. government obligations. Use Schedule K, Federal Form 1120S, as the source for the amounts of income and deductions.

LINE 5. Enter all interest income from state and local bonds which are exempt from federal tax and are not issued by Nebraska sources.

LINE 6, BONUS DEPRECIATION ADD-BACK. Multiply the total bonus depreciation claimed on the federal return by 85 percent (.85) and enter the result on line 6. This will allow the S corporation to withhold and remit the additional tax due for all nonresident individual shareholders who do not provide a completed Form 12N to the S corporation.

LINE 7, ENHANCED SECTION 179 EXPENSE DEDUCTION ADD-BACK. Subtract \$25,000 from the total enhanced Section 179 expense deduction claimed on the federal return and enter the result on line 7. This will allow the S corporation to withhold and remit the additional tax due for all nonresident individual shareholders who do not provide a completed Form 12N to the S corporation.

LINE 8. Enter any other additions to income for the S corporation that are includible in the shareholders' federal income but are not reflected in lines 1 through 7 above (attach schedule).

LINE 10. Enter income from obligations of the U.S. government exempt from state taxation. A listing of those U.S. government securities that are exempt may be obtained by reviewing Corporate Income Tax Regulation 24-048. Interest income from repurchase agreements involving U.S. government obligations **is not** deductible as U.S. government interest.

LINE 19. Enter any other deductions to income for the S corporation that are deductible in determining the shareholders' federal income but are not reflected in lines 10 through 18 above (attach schedule).

INSTRUCTIONS FOR NEBRASKA SCHEDULE III Nonresident Shareholder's Share of Bonus Depreciation, Enhanced Section 179 Expense Deduction, and Nebraska Income

An S corporation which has claimed federal bonus depreciation, enhanced Section 179 expense deduction or which has income derived from sources within Nebraska and has at least one nonresident shareholder who is an individual will complete Nebraska Schedule III. This schedule is not necessary when the corporation has a Nebraska loss; instead, attach a schedule showing each shareholder who owned stock during the taxable year, the dates of ownership, and the percent of ownership. Compute the share of the Nebraska loss by multiplying the loss by the percent of ownership for the portion of the year the stock was owned.

Nebraska Schedule III is also not necessary when all the corporation's shareholders are Nebraska residents.

Enter the name, address, and social security number of each nonresident individual shareholder. If additional space is needed, attach a schedule using the same format as Nebraska Schedule III. **This schedule is completed for nonresident individual shareholders only.**

COLUMN B. Enter the pro rata interest of each nonresident individual who was a shareholder during the corporation's taxable year.

COLUMN D. If a signed Nebraska Nonresident Income Tax Agreement, Form 12N, is attached, do not complete columns E and G.

COLUMN G. Enter 6.84 percent of column E, which is the amount of Nebraska income tax to be withheld for each nonresident individual shareholder. Report the amount withheld from each nonresident individual shareholder on a Statement of Nebraska Income Tax Withheld for Nonresident Individual, Form 14N. The total of column G must equal the amount entered on line 11, Form 1120-SN.